

TO: Files

CC: San Diego Audit Committee

FROM: Willkie Farr & Gallagher LLP

RE: Interview of David Schlesinger on June 15, 2006

DATED: June 22, 2006

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On June 15, 2006, Michael Shapiro, in Willkie Farr & Gallagher LLP's capacity as counsel to the Audit Committee, interviewed David Schlesinger, formerly from the Metropolitan Wastewater Department ("MWWD") by telephone. Mr. Schlesinger was not represented by counsel.

The following memorandum reflects my thoughts, impressions, and opinions regarding our meeting with David Schlesinger, and constitutes protected attorney work product. It is not, nor is it intended to be, a substantially verbatim record of the interview.

***Diversion of funds***

Mr. Schlesinger was read Exhibit 1, a February 16, 2001 e-mail from Eric Adachi to David Schlesinger re: "Fwd: Meeting." Mr. Shapiro asked Mr. Schlesinger whether he recalled the details of the e-mail. Mr. Schlesinger did not. Mr. Schlesinger said that at the time of the e-mail, he was trying to think of ways to save money and that is why he made the suggestion in the e-mail to replace the insurance policy with cash from the CIP programs. He noted that he had concerns about borrowing too much money, which would result in arbitrage penalties. He also said he suggested substituting the insurance as a way of saving money. Mr. Shapiro asked Mr. Schlesinger if the original diversion of funds noted in the e-mail actually occurred, and he said he did not know. Mr. Shapiro then asked whether the alternative approach Mr. Schlesinger suggested actually occurred, and he said it did not.

Mr. Shapiro asked Mr. Schlesinger if the e-mail raised any concerns regarding the possible original diversion of funds. Mr. Schlesinger said that since the auditor found his suggestion to divert funds to be inappropriate, it may have been inappropriate had the City originally diverted funds from the contingency reserve to the CIP program, as stated in the e-mail. Mr. Schlesinger reiterated that his goal was to only borrow enough money to keep the CIP program going, which was divergent with the goal of Shari Sacks' group, which was to try to obtain the best interest rate even if it meant borrowing more money to achieve a lower rate. Mr. Shapiro asked Mr. Schlesinger if he could share any more insight regarding the insurance issue raised in the e-mail. Mr. Schlesinger said that Joe Harris or Bill Hanley may know more about it. Mr. Shapiro asked Mr. Schlesinger if he recalled any follow-up taking place after he received this e-mail. He did not.

***Conclusion***

Mr. Shapiro told Mr. Schlesinger to contact us if he recalled any new information in the future.

WF&G

3306160

# **EXHIBIT 1**

Email message text

Object type: [GW.MESSAGE.MAIL]

Item Source: [Sent]

Message ID: [3A8D3A8E.CAB7-9.FM.100.1383633.1.5EE2.1]

From: [Eric Adachi]

To: [;Dave Schlesinger;D5S.MW\_DEPT.MWWD]

Subject: [Re: Fwd: Meeting]

Creation date: [2/16/2001 2:34:54 PM]

In Folder: [Mail Box]

Attachments: None

Message: [

Dave,

Checked into your proposal; auditor's just informed me they had looked into it and discovered that it would be considered an inappropriate use of bond funds and therefore was not allowed.

Eric

>>> Dave Schlesinger 02/16 7:35 AM >>>

Eric - I believe a couple of years ago Shari Sacks received FA approval to divert funds from the contingency reserve to the CIP program in order to delay issue of the 1999 bonds. This action cost the sewer ratepayers \$800,000 (please verify this #) in terms of the insurance policy premium that replaced the cash in the reserve. If we are concerned about not meeting the final arbitrage goal (#3) why can't we simply replace the insurance policy with cash from the CIP program? Please provide a response before today's 4:00 PM meeting.

Dave

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TO: Files

CC: San Diego Audit Committee

FROM: Willkie Farr & Gallagher LLP

RE: Interview of David Schlesinger on June 20, 2006

DATED: June 20, 2006

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On June 20, 2006, Michael Shapiro, in Willkie Farr & Gallagher LLP's capacity as counsel to the Audit Committee, interviewed David Schlesinger, formerly from the Metropolitan Wastewater Department ("MWWD") by telephone. Johnny Giang and Tammie Davis from KPMG also participated in the interview. Mr. Schlesinger was not represented by counsel.

The following memorandum reflects my thoughts, impressions, and opinions regarding our meeting with David Schlesinger, and constitutes protected attorney work product. It is not, nor is it intended to be, a substantially verbatim record of the interview.

***NPDES Permit***

Mr. Shapiro asked Mr. Schlesinger if the City of San Diego had a Natural Pollutant Discharge Elimination System ("NPDES") permit for storm water discharge. Mr. Schlesinger replied that the City had a NPDES permit for Point Loma but did not have one for storm water while he worked for the City. Mr. Shapiro asked Mr. Schlesinger when he left the City's employment. Mr. Schlesinger responded that he retired in May 2001.

***"Inflow sources"***

Mr. Schlesinger was read Exhibit 1, a February 14, 2002 email from Bill Hanley (Deputy Director for Contract Services, MWWD) to Dennis Kahlie (Utilities Finance Administrator) and Kelly Salt (Chief Deputy City Attorney of the Public Works Section) re: "Revenue Program Guidelines," discussing the definition of "inflow sources" contained in a sewer use ordinance. Mr. Shapiro asked Mr. Schlesinger to explain Mr. Kahlie's email regarding "inflow sources." Mr. Schlesinger replied that historically, people in San Diego tried to connect their storm water flows to the sewage system. He said that unlike the East Coast that has a combined system for storm water and wastewater, San Diego has a dual system and the City is careful to make sure that no one's storm water is connected to the wastewater system. Mr. Schlesinger noted that if someone connected their storm water flow to the sewage system, they would be charged a capacity fee.

Mr. Shapiro asked Mr. Schlesinger to explain the "\$410 million" referenced in the email. Mr. Schlesinger did not know. Mr. Shapiro asked Mr. Schlesinger if the number possibly represented the amount of grants and loans the City had obtained. Mr. Schlesinger said that the

amount of grants and loans was “in that range.” Mr. Shapiro asked Mr. Schlesinger if it would concern him if people were connecting their storm water flows to the sewer system. Mr. Schlesinger replied that it would concern him because “you can’t give people a free ride” if the City is obtaining grants and loans. Mr. Shapiro asked Mr. Schlesinger if he had any particular concerns about the “inflow sources” issue. Mr. Schlesinger responded that when it came to the Convention Center, the Center was pumping storm water into the sanitary sewage system; however, the Center was charged for doing so. Mr. Shapiro asked Mr. Schlesinger whether paying for having storm water flow into the sewer system was appropriate and in compliance with federal and state law. Mr. Schlesinger replied that those entities that connected their storm water flow to the sewer system paid as if they were discharging sewage and thus, the City maintained compliance. He said that as long as users were charged in proportion to their use, the City complied with the Clean Water Act and the City’s loans and grants. Mr. Shapiro asked Mr. Schlesinger what Mr. Hanley meant in the email when he wrote “You’re nothing but good news.” Mr. Schlesinger replied that he believed Mr. Hanley was upset by the news shared by Mr. Kahlie. Mr. Shapiro asked Mr. Schlesinger if he was aware of any violation of federal, state or city laws regarding inflow sources. Mr. Schlesinger said that he was not.

Mr. Giang asked Mr. Schlesinger whether any sewage was placed in the storm water drainage. Mr. Schlesinger replied, “no, never” and explained that the City “would never utilize that.” Mr. Schlesinger noted that there is a “first flush” system in San Diego, a series of pumps to prevent storm water from going into the ocean. He said that the “first flush” system raised no issue in his mind with regard to any federal, state or city laws. He noted that the “first flush” system received some State funding for its construction.

### ***Conclusion***

Mr. Shapiro told Mr. Schlesinger to contact us if he recalled any new information in the future.

WF&G

# **EXHIBIT 1**

158773

Email message text

Object type: [GW.MESSAGE.MAIL]

Item Source: [Received]

Message ID: [416BE3F7.Demo-dom.Demo-PO.100.1357474.1.27B.1]

From: [Bill Hanley]

To: []

Subject: [Re: Revenue Program Guidelines]

Creation date: [2/14/2002 7:04:29 PM]

In Folder: [Sewer Cost of Service]

Attachments: None

Message: [

Kahlie - You're nothing but "good" news.

>>> Dennis Kahlie 02/14/2002 4:14:26 PM >>>

Great! While you're at it, you might want to read the section on the sewer use ordinance, which requires that we prohibit any new connections from "inflow sources". "Inflow sources" is a defined term which includes cross connections between sanitary and storm sewers, storm water, surface runoff and other stuff that certain people want to put in the sewer system - another great reason to give that \$410 million back.

- D

>>> Kelly Salt 02/14 3:56 PM >>>

Thanks Dennis. Per the closed session discussion, I am currently reviewing these issues.

>>> Dennis Kahlie 02/14/02 03:51PM >>>

The attached file includes all SRF loan program documents. The latest (2/21/96) version of the Revenue Program Guidelines is included as appendix G.

- D

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